



The Irrevocable Income Only Trust

By: Brian F. Mahoney, Esq.



An often discussed mechanism in Medicaid/Nursing Home planning is the IIOT, an Irrevocable Income Only Trust.

Aside from Nursing Home issues and look back periods we need to first ask about financing issues. Consider whether the Trustee might ever need to obtain financing on the realty, perhaps for a new burner or roof. Most Lenders will not mortgage realty owned by any irrevocable Trust. Would deeding realty into an IIOT make a pre-existing mortgage due and payable?

If the sale of realty after it is deeded into the IIOT is a possibility we can structure the IIOT as a Grantor Trust. If an Elder Trustmaker later moves into Assisted Living or into a Nursing facility, there is no spouse at home and that realty is sold by the Trust, we want the Trustmaker to be able to elect the \$250K capital gain exclusion.

To that end I insert a testamentary power of appointment allowing the Trustmaker to appoint Trust property by Will to a class of persons described in the IIOT. I do not include a lifetime power to appoint because it may be considered too much power in the skeptical eye of a Medicaid case-worker especially in this era of recession. Their position might be this would render the IIOT a "Medicaid qualifying trust." It can be overcome but do we want to go into the trial Court to refute their arguments?

The Trustmaker should have no power to appoint trust principal to himself, his creditors, his estate or his estate's creditors. The ultimate goal of an IIOT is for Trust owned assets to be non-countable and the less the IIOT contains for "escape mechanisms," the more certain our objective becomes.

We do provide an "escape hatch," in the IIOT in case the look back period is not met to avoid the worst of both worlds (i.e. principal that is "countable") for Medicaid

purposes, but which cannot be accessed by the Trustmaker. Provide for appointment of a Trust Protector who could be a corporate fiduciary, Attorney, C. P. A. or an individual who is not related or subordinate to a transferor or any Beneficiary within the meaning of Section 672(c) of the Internal Revenue Code.

The IIOT may provide that during the Trustmaker's lifetime the Trust Protector may in writing, direct the Trustee to pay to or apply for the benefit of the children or grandchildren of the Trustmaker or their spouses, so much of trust principal as the Trust Protector in its sole discretion deems advisable.

To preserve Grantor Trust status then, along with the testamentary POA and "Trust Protector escape hatch," we need to add a so-called Designating Person who can add a class of Beneficiaries. The class might consist of: children, grandchildren, spouses, or charities. The Trustmaker, the Trust Protector, any Beneficiary of the IIOT (including any person who may be added as a Beneficiary) any so-called "adverse party," as defined in Section 672(a) of the Code, or any so-called "related or subordinate party," as defined in Sect. 672(c) of the Code should not be appointed to serve as a Designating Person.

Can the Trustmaker(s) be Trustee? There appears to be no express prohibition against that, but with the current government deficits and budget cuts, why risk a higher level of scrutiny. If we have decent prospects as Trustee it may be safer to not have the Trustmaker in the position of power as a Trustee.

We all know the number of potential Adult Child/Trustee pitfalls that can develop. Will the existence of the Trustmaker's testamentary POA be enough to keep an Adult Child/Trustee in line if he can be "disinherited," from the very Trust that Child administers?

Include a provision allowing the Trustmaker to remove any

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Trust Protector or Trustee with or without cause at any time to allow the Trustmaker some much needed control in the event a relationship with a fiduciary sours in the future. Is that too much power for Medicaid? Can a Client afford not to have such removal powers?

Many practitioners are now acting as Trustees or Trust Protectors for their Clients' IIOT's knowing they'll never act in a manner contrary to the Trustmaker's best interests.

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